REPORT OF EXAMINATION
OF THE

FARMERS INSURANCE EXCHANGE

AS OF
DECEMBER 31, 2009

Participating State
and Zone:

California

Filed June 28, 2011

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Los Angeles, California
May 9, 2011

Honorable Joseph Torti, III
Chairman of the NAIC Financial
Condition Subcommittee
Superintendent of Rhode Island Business
Regulation, Division of Insurance
Cranston, Rhode Island

Honorable Linda S. Hall
Secretary, Zone IV – Western
Director of Insurance
Alaska Division of Insurance
Anchorage, Alaska

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Secretary, and Commissioner:

Pursuant to your instructions, an examination was made of the

FARMERS INSURANCE EXCHANGE

(hereinafter also referred to as the Exchange) at its statutory home office and main administrative office located at 4680 Wilshire Boulevard, Los Angeles, California 90010.

SCOPE OF EXAMINATION

The previous examination of the Exchange was made as of December 31, 2006. This examination covers the period from January 1, 2007 through December 31, 2009. The examination was made pursuant to the National Association of Insurance Commissioners' plan of examination. The examination included a review of the Exchange's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2009, as deemed necessary under the circumstances. This examination was conducted concurrently with certain of the Exchange's California subsidiaries and affiliates, namely: Fire Insurance Exchange, Truck Insurance

Exchange, Mid-Century Insurance Company, Civic Property and Casualty Company, Exact Property and Casualty Company, Neighborhood Spirit Property and Casualty Company, and Farmers Reinsurance Company.

The California Department of Insurance was the lead state in this coordinated examination of the aforementioned companies, six non-California reinsurance pool participant companies, eighteen companies of the 21st Century Insurance and Financial Services (formerly AIG) personal auto group (21st Century), and five companies of the Bristol West Holdings, Inc. (Bristol West) group. The 21st Century group and the Bristol West group are further identified in the Exchange History section of this report.

In addition to those items specifically commented upon in this report, other phases of the Exchange's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; accounts and records; and sales and advertising.

SUBSEQUENT EVENTS

Farmers Group, Inc. (FGI), the Exchange's attorney-in-fact, entered into a settlement agreement on December 12, 2010, regarding a class-action lawsuit identified as Fogel versus FGI, Truck Underwriters Association (TUA), as the attorney-in-fact for Truck Insurance Exchange (Truck), Fire Underwriters Association (FUA), as the attorney-in-fact for Fire Insurance Exchange (Fire), and Zurich Financial Services Ltd. "Fogel" consists of a class of certain Exchange, Fire and Truck policyholders as identified for certain previous policy years. The litigation primarily involves subscription fees (management fees) paid by the policyholders to their respective attorney-in-fact. The total potential settlement amount, if all qualifying policyholders file claims, is $455 million to be paid by FGI, TUA, and FUA. Up to $90 million is additionally established by the settlement agreement for payment to plaintiff's attorneys upon court approval. A number of initiatives at FGI, TUA, and FUA are included in the settlement agreement to further raise standards of customer communication. These include providing welcome packs and additional disclosures to Exchange policyholder-subscribers and providing additional training to its agents and front-line employees regarding the subscription agreement and related procedures.

The three Exchanges are not defendants in the lawsuit but are involved because the plaintiffs in the class-action suit are their policyholders, and because any remaining portion of the settlement amount (the amount not claimed by specific policyholders) will be paid by FGI, TUA, and FUA to the Exchanges per this agreement. A final approval hearing for this settlement agreement is set for September 7, 2011.

EXCHANGE HISTORY

The Exchange was organized in the State of California on September 28, 1928, for the purpose of conducting property and casualty insurance.

A significant portion of the Exchange's reported surplus as regards policyholders at the examination date was composed of surplus notes, issued to non-affiliates, and contribution certificates, issued to affiliates. The following schedule depicts the specific issuances and par value amounts outstanding at December 31, 2009:

	Date Issued	Interest Rate	Par Value	Maturity Date
1)	5/11/1994	8.625%	$ 300,000,000	5/01/2024
2)	7/10/1998	7.050%	373,077,000	7/15/2028
3)	7/10/1998	7.200%	111,923,000	7/15/2048
4)	6/21/2004	6.150%	280,000,000	12/31/2013
5)	8/09/2004	6.000%	100,000,000	8/01/2014
6)	12/23/2004	6.150%	296,000,000	8/01/2014
7)	12/31/2008	10.270%	300,000,000	12/31/2013
	Total		$1,761,000,000	

The aforementioned notes and certificates have restrictions, which require the approval of the California Department of Insurance (CDI) before payment of any interest and principal. Interest can be paid out of earned (unassigned) surplus only. The payments of interest and repayments of principal, occurring during this examination period were made with the approval of the CDI. The carrying value of the above notes is $1,760,675,000 at December 31, 2009.

Items 1), 2), and 3) are surplus notes, transacted in 1994 and 1998, and issued to qualified institutional buyers in the open market and administered by JP Morgan Chase Bank.

Item 4) is a certificate of contribution in the amount of $280 million issued to Zurich Capital Markets, Inc. (ZCM) on June 21, 2004 in consideration for its surrender and discharge of certain certificates originally issued on November 15, 2001, but assigned by Farmers Group, Inc. (FGI) to ZCM on January 30, 2004. On July 28, 2004, the certificate was assigned by ZCM to Zurich Investments LLC (ZIL), a Luxembourg company. On January 17, 2008, the certificate was assigned by ZIL to Zurich American Insurance Company.

Item 5) represents surplus notes in the amount of $100 million that were issued on August 9, 2004 to qualified institutional buyers in the open market and are administered by JP Morgan Chase Bank. These notes replaced $100 million of surplus notes that were issued during 1994 and matured on August 2, 2004.

Item 6) is a $296 million certificate of contribution issued to Farmers New World Life on December 23, 2004 as part of a refinancing transaction in which the Exchange canceled the certificates originally issued on March 7, 2000. The certificates were transferred to FGI on October 10, 2005, and subsequently transferred to Zurich Group Holdings on November 21, 2005.

Item 7) is a $300 million certificate of contribution issued to Farmers Reinsurance Company on December 31, 2008 in exchange for cash.

On December 31, 2009, the Exchange's subsidiary, Foremost Corporation of America (Foremost Corp.), was merged into FCOA, LLC, a non-insurance entity formed in 2009 and owned by the Foremost Insurance Company Grand Rapids, Michigan (Foremost I.C.), with FCOA, LLC as the surviving entity. All outstanding common shares of Foremost Corp. were retired and Foremost I.C. issued new common shares to the Exchange.

Bristol West Holdings, Inc.

On July 3, 2007, Farmers Group, Inc. (FGI) completed the acquisition of Bristol West Holdings, Inc. (BWH), a Delaware corporation, including its two directly-owned insurance company subsidiaries: Security National Insurance Company, a Florida company, and Bristol West Preferred Insurance Company, a Michigan company. Also included in the acquisition were certain insurance services companies and BWH's directly owned insurance holding company: Coast National Holding Company, a California company, and its insurance company subsidiary Coast National Insurance Company (CNIC), also a California company, which in turn owned Bristol West Insurance Company, an Ohio company, and Bristol West Casualty Insurance Company, an Ohio company. Concurrent with the acquisition, FGI sold BWH and its subsidiaries and underlying insurance business to the Exchange, Truck Insurance Exchange (Truck), Fire Insurance Exchange (Fire), and Mid-Century Insurance Company (Mid-Century).

BWH, via its insurance subsidiaries, had licenses in 38 states plus the District of Columbia, and operated in 22 states and as a provider of liability and physical damage insurance, specializing in non-standard private passenger auto.

FGI paid $713.5 million and assumed $100 million of debt obligations as consideration for the acquisition of BWH. Additional consideration for the transaction included the "commutation of certain existing affiliated reinsurance arrangements" between BWH's insurance subsidiaries, and the execution of a 90% quota share cession agreement between CNIC and the Exchange effective January 1, 2007. This quota share treaty was replaced with a 100% quota share agreement, effective July 1, 2008. The 100% CNIC quota share agreement was approved by the CDI August 15, 2008.

The Exchange also entered into a similar 90% quota share agreements with BWH's affiliates: Bristol West Insurance Company (Ohio), Bristol West Casualty Insurance Company (Ohio), Bristol West Preferred Insurance Company (Michigan), and Security National Insurance Company (Florida).

The acquisition of BWH resulted in changes in the ultimate control of BWH's subsidiary, CNIC. The Exchange and Zurich Financial Services Ltd. (ZFS), a Swiss company and FGI's ultimate parent corporation, filed a joint Form A application pursuant to California Insurance Code (CIC) Section 1215.2. Additionally, Form D applications were filed pursuant to CIC 1215.5. The CDI approved the transactions on June 28, 2007.

FGI sold BWH and its subsidiaries and underlying insurance business to the Exchange, Truck, Fire, and Mid-Century for $420 million, which represented an equity value of $370 million plus $50 million of debt assumption. In addition, the Exchange, Truck, Fire, and Mid-Century incurred transaction fees of $13.8 million. FGI retained certain of BWH's employees, the operational systems, and the management servicing rights. The acquisition was recorded using the statutory purchase method of accounting. The following schedule depicts each exchange/company's share of the costs, fees and goodwill for the acquisition of the BWH insurance business at the time acquired:

	(in millions)		
Entity	Cost and Fees	Goodwill	Percentage
Farmers Insurance Exchange	$162.7	$38.2	37.50%
Truck Insurance Exchange	38.0	8.9	8.75%
Fire Insurance Exchange	16.3	3.8	3.75%
Mid-Century Insurance Company	216.8	51.0	50.00%
Totals	$433.8	$101.9	100.00%

On September 30, 2008, the Exchange acquired an additional 4.5% ownership interest in BWH; 2.5% acquired from Mid-Century for $12.3 million and 2.0% acquired from Truck for $9.8 million.

On September 30, 2008, the following additional transactions were made between the three exchanges:

(1) The Exchange sold all of its 80% ownership interest in Civic Property and Casualty Company, Exact Property and Casualty Company, and Neighborhood Spirit Property and Casualty Company to Truck and Fire for $182.9 million.

(2) The Exchange sold 5% and 10% of its ownership interest in Mid-Century and Farmers Insurance Company of Oregon for $34.9 million and $43.0 million, respectively to Truck.

<u>Purchase of AIG personal auto business:</u>

On July 1, 2009, Farmers Group, Inc. (FGI) completed the acquisition of the American International Group, Inc.'s personal auto group of companies. This included the personal auto business of 21st Century Insurance Group. FGI paid $1.9 billion plus solely assumed $100 million of 21st Century Insurance Group's outstanding debt. Concurrent with the transaction FGI sold the personal auto group companies and underlying insurance business to the Exchange, Truck, and Fire for $1.39 billion. FGI retained certain of the personal auto group employees, the operational systems, and the management servicing rights. In addition, the Exchange, Truck, and Fire incurred transaction fees of $6 million and also contributed $55 million of additional paid-in capital. The CDI approved these transactions on June 26, 2009.

As a consequence of this acquisition the Exchanges now own, either directly or indirectly, the following insurers: 21st Century Casualty Company, 21st Century Insurance Company, 21st Century Insurance Company of the Southwest, AIG Centennial Insurance Company, AIG Auto Insurance Company of New Jersey, AIG Preferred Insurance Company, AIG Premier Insurance Company, AIG Indemnity Insurance Company, AIG Hawaii Insurance Company, Inc., American Pacific Insurance Company, Inc., AIG Advantage Insurance Company, American International Insurance Company of California, Inc., American International Insurance Company of New Jersey, American International Insurance Company of Delaware, American International Pacific Insurance Company, New

Hampshire Indemnity Company, Inc., AIG National Insurance Company, Inc., and American International Insurance Company.

Concurrent to this acquisition a 100% quota share reinsurance agreement was entered into between American International Insurance Company (New York) and the Exchange to be effective July 1, 2009. This 100% quota share agreement was approved by the CDI on June 30, 2009.

The following 21st Century Companies officially changed their names effective April 1, 2010. The name change was filed with and approved by the requisite regulatory authorities.

Current Name	Formerly Doing Business As
21st Century Advantage Insurance Company	AIG Advantage Insurance Company
21st Century Assurance Company	American International Insurance Company of Delaware
21st Century Auto Insurance Company of New Jersey	AIG Auto Insurance Company of New Jersey
21st Century Centennial Insurance Company	AIG Centennial Insurance Company
21st Century Indemnity Insurance Company	AIG Indemnity Insurance Company
21st Century National Insurance Company	AIG National Insurance Company, Inc.
21st Century North America Insurance Company	American International Insurance Company
21st Century Pacific Insurance Company	American International Pacific Insurance Company
21st Century Pinnacle Insurance Company	American International Insurance Company of New Jersey
21st Century Preferred Insurance Company	AIG Preferred Insurance Company
21st Century Premier Insurance Company	AIG Premier Insurance Company
21st Century Security Insurance Company	New Hampshire Indemnity Company, Inc.
Farmers Insurance Hawaii, Inc. *	AIG Hawaii Insurance Company, Inc.

*Effective January 1, 2010

Surplus Loan Note Facility

The Exchange entered into a "Credit Agreement" dated July 10, 2007 with certain European lending banks. This agreement was arranged by Swiss Reinsurance Company, a Swiss company.

Commerzbank International S.A., a Luxembourg company acted as Administrative Agent for the European banks. Pursuant to this credit agreement, the lenders committed to purchase Surplus Loan Notes from the Exchange, up to an aggregate principal amount not in excess of $500 million, based on a Trigger Event (catastrophic windstorm losses in excess of $1.5 billion incurred losses in the states of Arkansas, Louisiana, Oklahoma, and/or Texas). The commitment termination date is July 10, 2012.

The Surplus Loan Notes would be subordinated obligations of the Exchange with a 10 year final maturity. Payment of principal and interest on the Surplus Loan Notes would require the approval of the CDI. The fees paid by the Exchange for rights to access this facility were $9.8 million for 2007, $2.5 million for 2008, and $2.5 million for 2009.

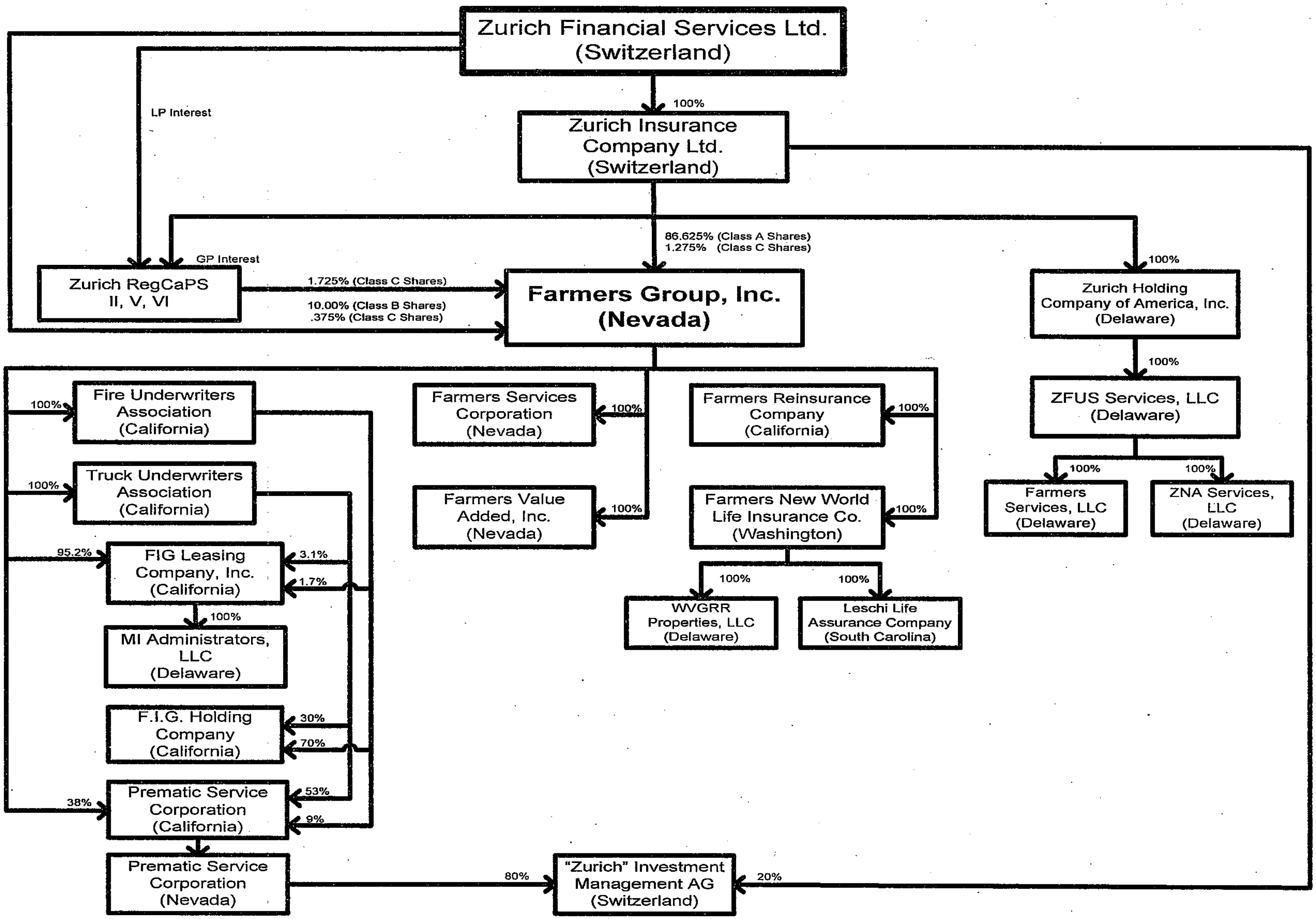
This credit agreement establishes an advance facility to assure the placement of reasonably-priced surplus notes or certificates of contribution, to re-capitalize the Exchange in the event of a catastrophic windstorm event to augment the layers of reinsurance.

MANAGEMENT AND CONTROL

The Exchange, a reciprocal insurer organized under California Insurance Code (CIC) Section 1300 et. seq. is controlled by its attorney-in-fact, Farmers Group, Inc. (FGI), dba Farmers Underwriters Association. FGI is a U.S. subsidiary of Zurich Financial Services Ltd. (ZFS), a Swiss holding company.

On May 8, 2008, the intermediate-level holding structure was re-organized and FGI became owned 87.9% by Zurich Insurance Company (ZIC), 10.375% by Zurich Group Holdings (ZGH), and 1.725% by three Partnerships (Zurich RegCaPs II, V, VI) having ZIC as the General Partner and ZGH as the Limited Partner. On November 30, 2009, another restructuring occurred, as a result of which FGI became directly owned 87.9% by ZIC, 10.375% by ZFS, and 1.725% by three Partnerships (Zurich RegCaPs II, V, VI). ZFS continues to be the ultimate controlling party.

The following abridged organizational chart show the relationships of the attorney-in-fact FGI to its ultimate parent ZFS, and of the three Exchanges to their affiliates as of December 31, 2009:



Zurich Financial Services Ltd. (Switzerland)
100%
Zurich Insurance Company Ltd. (Switzerland)
LP Interest
GP Interest
Zurich RegCaPS II, V, VI
1.725% (Class C Shares)
10.00% (Class B Shares)
.375% (Class C Shares)
86.625% (Class A Shares)
1.275% (Class C Shares)
Farmers Group, Inc. (Nevada)
100%
Zurich Holding Company of America, Inc. (Delaware)
100%
ZFUS Services, LLC (Delaware)
100%
Farmers Services, LLC (Delaware)
100%
ZNA Services, LLC (Delaware)
100%
Fire Underwriters Association (California)
100%
Truck Underwriters Association (California)
95.2%
FIG Leasing Company, Inc. (California)
3.1%
1.7%
100%
MI Administrators, LLC (Delaware)
30%
70%
F.I.G. Holding Company (California)
38%
Prematic Service Corporation (California)
53%
9%
Prematic Service Corporation (Nevada)
100%
Farmers Services Corporation (Nevada)
100%
Farmers Value Added, Inc. (Nevada)
100%
Farmers Reinsurance Company (California)
100%
Farmers New World Life Insurance Co. (Washington)
100%
WVGRR Properties, LLC (Delaware)
100%
Leschi Life Assurance Company (South Carolina)
80%
"Zurich" Investment Management AG (Switzerland)
20%

FARMERS EXCHANGES ORGANIZATION

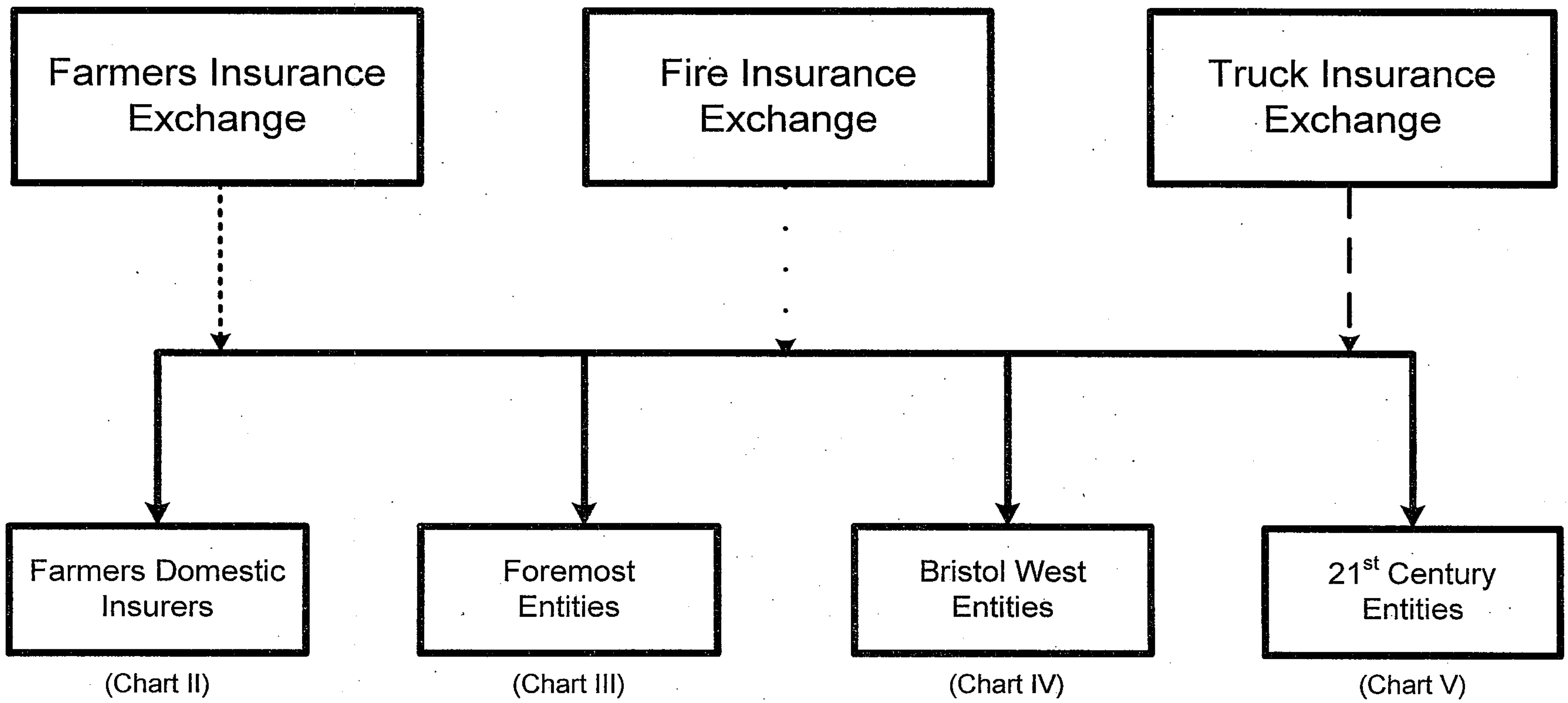


CHART II: EXCHANGES/FARMERS ENTITIES ORGANIZATION

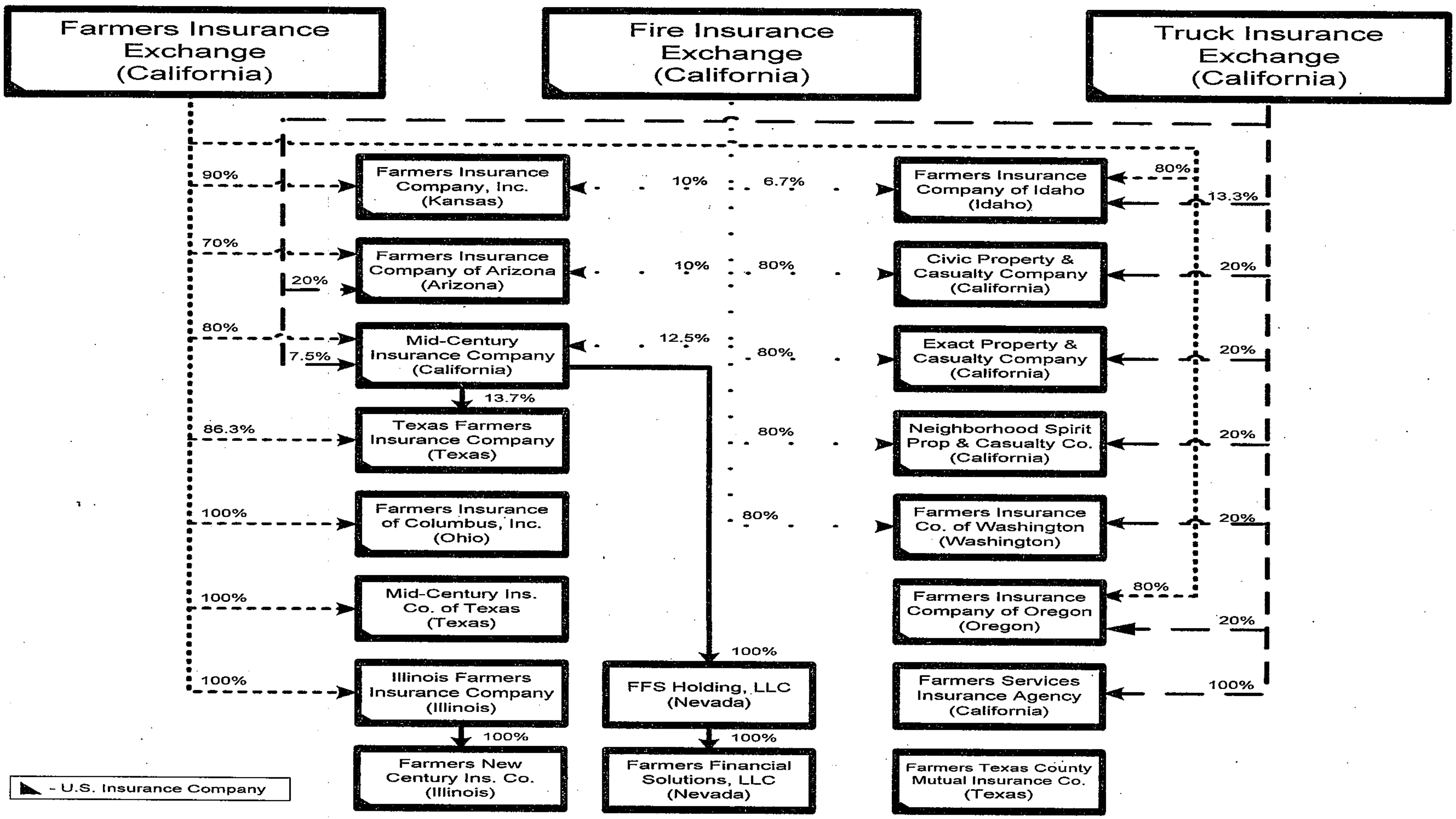
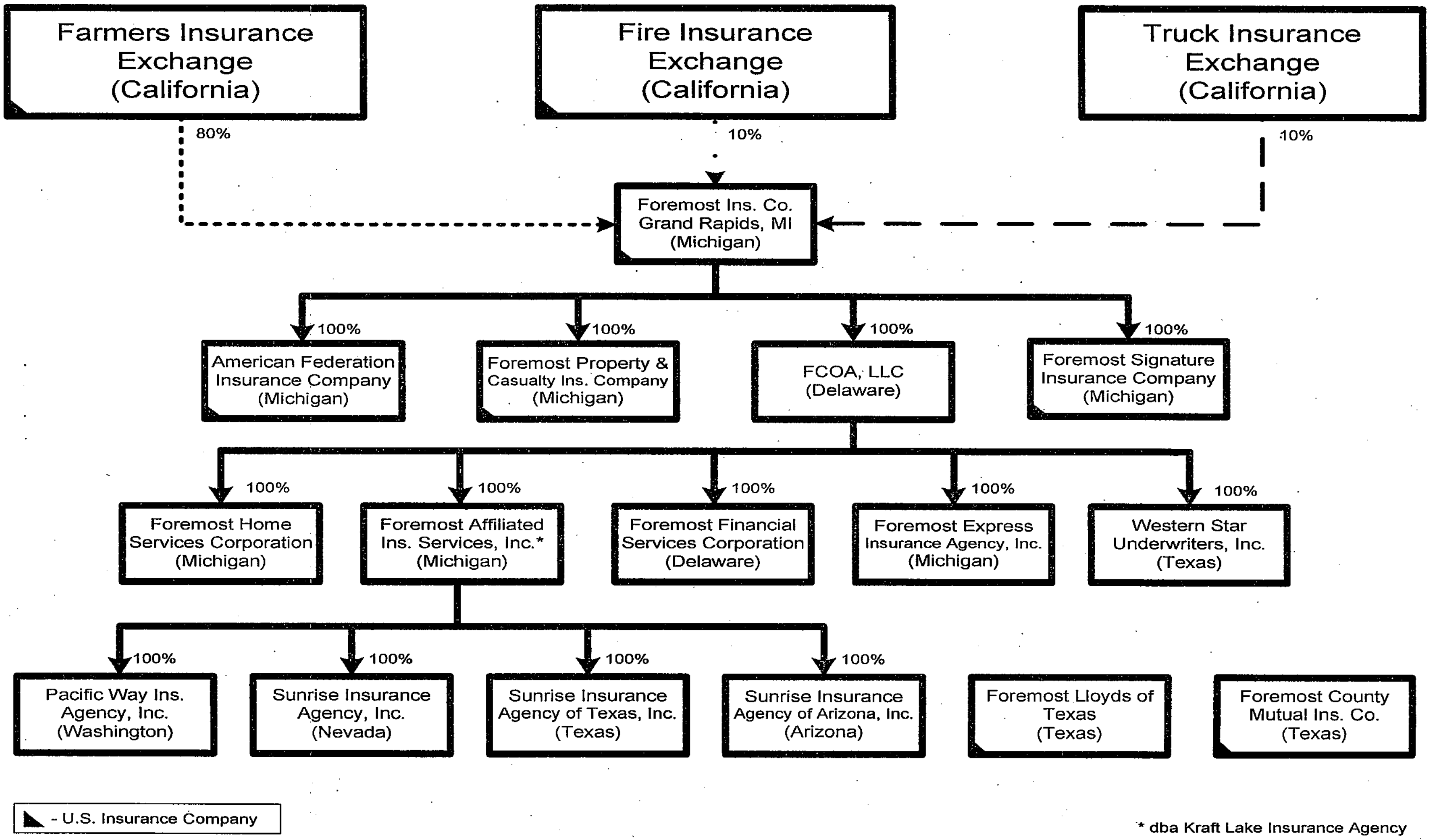
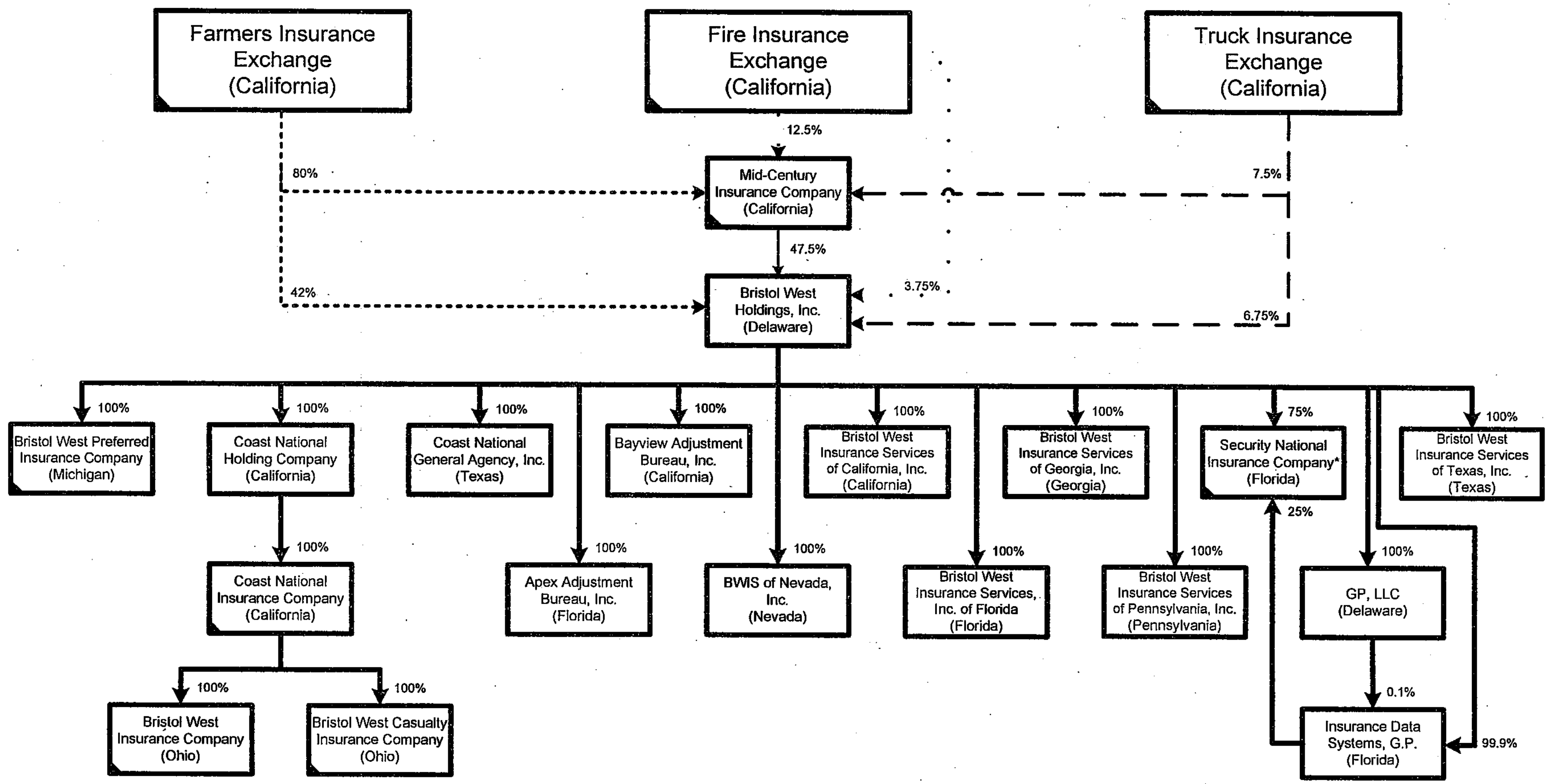


CHART III: EXCHANGES/FOREMOST ORGANIZATION



* dba Kraft Lake Insurance Agency

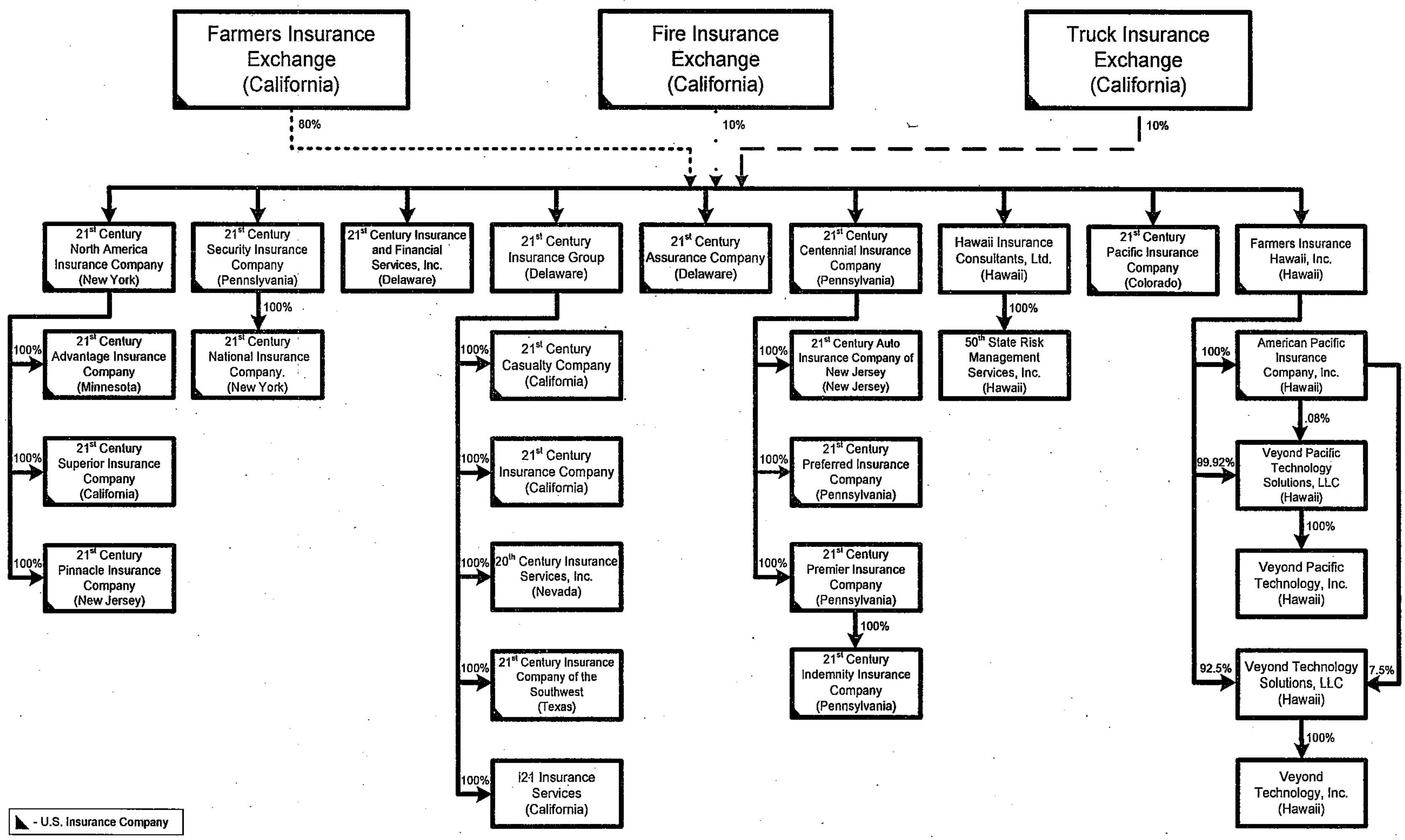
CHART IV: EXCHANGES/BRISTOL WEST ORGANIZATION



- U.S. Insurance Company

* Shares held by Bristol West Holdings, Inc. are voting shares, while those held by Insurance Data Systems, G.P. are non-voting shares

CHART V: EXCHANGES/21st CENTURY ORGANIZATION



The Exchange has a Board of Governors of not less than five nor more than twelve members. A listing of the members of the Board of Governors of the Exchange and principal officers of the Exchange and of its attorney-in-fact serving on December 31, 2009 follows:

Board of Governors

Name and Residence	Principal Business Affiliation
William Haskell Braddock Surprise, Arizona	Retired
Vince Stolte Garrod * Saratoga, California	Trustee and Manager Family Trust
Fredrick Henry Kruse Lake Ozark, Missouri	Retired
Dennis Joseph Lorch Advance, Missouri	Retired
Dale Anne Marlin Newport Beach, California	Retired
Ronald Lee Marrone Pittsburg, Kansas	Co-Owner Family Food Services Corporation
Donnell Reid Ballwin, Missouri	Retired
Donald Eugene Rodriguez Long Beach, California	Executive Director Boys and Girls Clubs
Taylor Lane Stephens ** Fort Collins, Colorado	Part-Time Consultant
Ottie Joel Wallace Merced, California	President Trucking and Logistics Company
John Tsu-Chao Wuo Arcadia, California	President Real Estate Agency

(*) Resigned on June 3, 2010, and was not replaced.
(**) Replaced by Gary Randolph Martin on March 22, 2010.

Principal Officers of the Exchange

Ronald Gregory Myhan	Vice President and Treasurer
Doren Eugene Hohl	Secretary

Principal Officers of the Attorney-in-Fact of the Exchange

Name	Title
F. Robert Woudstra	President and Chief Executive Officer
Doren Eugene Hohl	Secretary
Jerry Joseph Carnahan	Vice President
Jeffrey John Dailey	Vice President
Laszlo George Heredy	Vice President
Kevin Eugene Kelso	Vice President
Scott Robert Lindquist	Vice President
Bryan Francis Murphy	Vice President
James Leslie Nutting	Vice President
Constantine Paul Patsis	Vice President
Mhayse Gokul Samalya	Vice President

Management Agreements

FGI, as the attorney-in-fact, provides operating services (including staffing and occupancy), except claims adjustment services, to the Exchange. These services were provided to the Exchange pursuant to the "subscription agreements" entered into between the Exchange and each individual policyholder of the Exchange. There was no specific management services agreement required between the Exchange and FGI for the aforementioned services provided. CIC Sections 1215.4 and 1215.5 provide for an exemption from reporting for an inter-insurance exchange utilizing the subscription agreements providing that the "form of this agreement was in place prior to 1943 and it was not amended in any way to modify payments, fees, or waivers of fees or otherwise substantially amended after 1943". For 2007, 2008, and 2009, subscription fees forwarded by the Exchange to FGI for such services were $886,534,285, $971,924,280, and $1,086,365,475, respectively.

The Exchange is responsible for the payment of claims (adjustment function), payment of commissions, and the payment of premium and income taxes.

Management Services Agreements

The Exchange is a party to a management services agreement, effective May 15, 2009, with Mid-Century Insurance Company, an affiliate. The Exchange provides management services and claims adjusting services. This agreement was approved by the California Department of Insurance (CDI) on April 30, 2009.

The Exchange is a party to separate management services agreements, effective March 1, 2010, with Civic Property and Casualty Company, Exact Property and Casualty Company, and Neighborhood Spirit Property and Casualty Company, all affiliates. The Exchange provides management services and claims adjusting services. These agreements were approved by the CDI on January 22, 2010.

The Exchange is a party to a management services agreement, effective June 30, 2009, with 21st Century North American Insurance Company (formerly American International Insurance Company), (New York), an affiliate. The Exchange provides management services and claims adjusting services. This agreement was approved by the CDI on June 17, 2009. American International Insurance Company is the lead company in the personal auto group of eighteen insurance companies that were purchased from the American International Group, Inc. during 2009.

The Exchange is a party to various management services agreements, effective March 1, 2010, with fourteen non-California-domiciled affiliates, as follows: Farmers Insurance Company, Inc., Farmers Insurance Company of Arizona, Illinois Farmers Insurance Company, Farmers New Century Insurance Company, Farmers Insurance Company of Idaho, Farmers Insurance Company of Oregon, Farmers Insurance Company of Washington, Farmers Insurance Company of Columbus, Farmers Texas County Mutual Insurance Company, Mid-Century Insurance Company of Texas, Texas Farmers Insurance Company, Foremost Insurance Company of Grand Rapids, Michigan, Bristol West Insurance Company, Bristol West Preferred Insurance Company, Bristol West Casualty Insurance

Company, and Security National Insurance Company. The Exchange provides management services and claims adjusting services. These agreements were approved by the CDI on December 31, 2009. The Exchange is a party to a management services agreement, effective September 3, 2009, with Coast National Insurance Company, an affiliate. Under this agreement, the Exchange provides management services and claims adjusting services. This agreement was approved by the CDI on September 2, 2009.

Regarding the aforementioned management services agreements and the following claims adjustment services agreements; the Exchange shall provide or arrange for the provision of services at its costs, and allocated in accordance with the methods prescribed in the NAIC Accounting Practices and Procedures Manual – SSAP 70. Amounts are to be determined and settled monthly.

Claims Adjustment Services Agreements

The Exchange staffs a claims department for the adjustment of its own claims and to adjust certain of its affiliated insurance companies' claims. During 2009 and 2010 the Exchange and certain affiliates (the pooled companies) entered into written management services agreements that include claims adjustment services to be provided by the Exchange.

The Exchange is also a party to separate claims adjustment services agreements with Fire Insurance Exchange and Truck Insurance Exchange, both dated August 25, 1964. These two agreements were amended and restated effective June 1, 1966.

Managed Care Services Agreement

The Exchange is a party to a managed care services agreement, effective October 1, 1998, with Zurich Services Corporation (ZSC), an affiliate. ZSC provides certain bill review and medical management services for the Exchange's workers' compensation claims. It was recommended in the previous examination that the Exchange submit the managed care services agreement to the CDI, pursuant to CIC Section 1215.5, for approval. The submission of the ZSC managed care services agreement was still pending as of this examination date. Subsequently, the Exchange and ZSC have, via amendment, terminated the existing agreement (except for case management services) effective July 15, 2010. A replacement managed care services agreement with Corvel Healthcare Corporation (unaffiliated) is currently near completion. During 2007, 2008, and 2009, service fees paid by the Exchange to ZSC as a result of its participation in the existing managed care services agreement were $600,000 for each year.

Tax Sharing Agreement

The Exchange's federal income tax return was consolidated with various insurance and non-insurance affiliates and subsidiaries. There was a long-standing written tax sharing agreement in place. The agreement was amended on July 25, 2000 to add Foremost Corporation of America (Foremost) and certain of its subsidiaries. A subsequent amendment, effective July 3, 2007, added Bristol West Holdings, Inc. and all of its subsidiaries, plus two companies owned by Foremost. The tax allocation was based on separate return calculations with current credit for net losses. On January 3, 2008, the CDI approved the July 3, 2007, amendment. A revised tax sharing agreement is pending, with an effective date of July 1, 2009, to include the recently acquired eighteen Personal Auto Group companies. The recently CDI approved (August 17, 2010) tax sharing agreement between Fire Insurance Exchange and an affiliate was used as a template for the new agreement for the Exchange, and the CDI indicated no separate approval of this additional agreement was necessary. The latest tax sharing agreement is also based on separate return calculations. The Exchange's portion of the federal income taxes paid or recovered for 2007, 2008, and 2009, was $41,482,000, ($149,290,000) and $10,252,000, respectively.

Investment Management Agreements

FGI, acting on behalf of the Exchange, Fire, Truck and the subsidiaries of these three Exchanges, entered into an Investment Management Agreement dated July 1, 1998 with its affiliate, Scudder Kemper Investments Inc. (Scudder). In 2002, Scudder was acquired and replaced by Deutsche Asset Management (DeAM), a division of Deutsche Bank, AG. DeAM, a non-affiliate, managed the fixed income and equity asset portfolios of the Exchange, Fire, Truck and the subsidiaries. The terms of the agreement have otherwise not been altered.

FGI was also a party to the Service Level Agreement dated November 4, 1998 with Scudder, which was replaced in 2002 by DeAM. DeAM, a non-affiliate, provided accounting and reporting services in connection with the Exchange, Fire, Truck and the stock subsidiaries' investment portfolios, including Securities Valuation Office reporting. DeAM was given the authority to vote the proxies of the common stock. The terms of the Service Level Agreement were left unchanged except for the replacement of parties.

Securities Lending Agreement

In 1999 the Exchange filed with the CDI a securities lending agreement with an affiliate, Zurich Capital Markets Trust Company (Zurich). In December 2001, the Exchange changed its securities lending agent from Zurich to the Bank of New York Western Trust (BNY), a non-affiliate, as Zurich exited the securities lending business. "Collateral" is defined in the securities lending agreement as government securities and cash. The agreement also stipulated that BNY establish a "custodial custody account" in the name of the Exchange for the purpose of holding collateral and approved investments pertaining to securities lending transactions. The custodian was Wall Street Portfolio Advisors, a division of BNY. The agreement was amended and restated, effective May 24, 2005. The agreements conformed to the securities lending limits specified in CDI Bulletin 82-2.

TERRITORY AND PLAN OF OPERATION

The Exchange is licensed to transact insurance business in the District of Columbia and the following 45 states:

Alabama	Kansas	Nevada	Tennessee
Arizona	Kentucky	New Hampshire	Texas
Arkansas	Louisiana	New Jersey	Utah
California	Maine	New Mexico	Vermont
Colorado	Maryland	North Carolina	Virginia
Delaware	Massachusetts	North Dakota	Washington
Florida	Michigan	Ohio	West Virginia
Georgia	Minnesota	Oklahoma	Wisconsin
Idaho	Mississippi	Oregon	Wyoming
Illinois	Missouri	Rhode Island	
Indiana	Montana	South Carolina	
Iowa	Nebraska	South Dakota	

Major Lines of Business:

The Exchange, and its pooled subsidiaries and affiliates, write most of the property and casualty lines of business with a heavy emphasis on personal lines. The principal lines written or assumed by the Exchange (the lead pooling company in the pooling arrangement) were private passenger auto liability, auto physical damage, and homeowners multiple peril. By volume, commercial multiple peril, and to a lesser extent, commercial auto liability writings were the more material commercial lines being written. In 2009, the Exchange wrote $3.2 billion of direct premiums. Of the direct premiums written, $982.7 million (30.7%) was written in California, $335.8 million (10.5%) was written in Colorado, $257.0 million (8.0%) was written in Texas, and $1.6 billion (50.8%) was written in the remaining states.

Personal and commercial business is produced for the Exchange and affiliated property and casualty companies by an exclusive agency force of about 15,000 agents and was supported by 28 state executive offices, 7 service centers, and about 270 branch offices responsible for handling claims.

REINSURANCE

Intercompany Reinsurance Pooling Agreement

The Exchange, and certain affiliates, participate in an intercompany reinsurance pooling agreement. Under this agreement, the affiliated participants ceded all of their business, net of reinsurance, to the Exchange (the lead company). The Exchange then retroceded a share of the business back to certain participants based on percentages prescribed under the pooling agreement. The last amendment to this long-standing agreement was approved by the California Department of Insurance (CDI) on January 12, 1999.

The participants in the intercompany reinsurance pooling agreement, and their respective participation percentages as of December 31, 2009, were as follows:

Pool Participant	Percentage
Farmers Insurance Exchange	51.75
Mid-Century Insurance Company	16.00
Truck Insurance Exchange	7.75
Fire Insurance Exchange	7.50
Farmers Insurance Company of Oregon	7.00
Farmers Insurance Company of Washington	2.00
Civic Property and Casualty Company	1.00
Exact Property and Casualty Company	1.00
Neighborhood Spirit Property and Casualty Company	1.00
Texas Farmers Insurance Company	1.00
Farmers Insurance of Columbus, Inc.	1.00
Farmers Insurance Company, Inc.	0.75
Illinois Farmers Insurance Company	0.75
Farmers New Century Insurance Company	0.75
Farmers Insurance Company of Idaho	0.75
Total	100.00

Assumed

Pursuant to long-standing 100% quota share reinsurance agreements, the Exchange also assumed business from certain members of the affiliated property and casualty companies which did not participate in the intercompany reinsurance pooling program as follows: Farmers Insurance Company of Arizona (1970); Mid-Century Insurance Company of Texas (1987); Farmers Texas County Mutual Insurance Company (1993); Maryland Casualty Company (1999); and Foremost Insurance Company Grand Rapids, Michigan (Foremost I.C.) (2000). As a result of the inter-company reinsurance pooling agreement and the reinsurance assumed agreements, the Exchange assumed 100% of the business written by all members of the Farmers Group Companies.

Effective January 1, 2000, via a quota share agreement, the Exchange assumed 100% of Foremost I.C.'s in-force business as of that effective date and 100% of renewal and new business after the effective date. This agreement was approved by the CDI on August 10, 2000.

Effective January 1, 2007, via a quota share agreement the Exchange began assuming 90% of Coast National Insurance Company's business (CNIC), a Bristol West Holdings, Inc. company. The CDI approved this agreement on June 29, 2007. This quota share treaty was replaced with a 100% quota share agreement to be effective July 1, 2008. The 100% CNIC quota share agreement was approved by the CDI on November 14, 2008.

Effective January 1, 2007, via separate quota share agreements, the Exchange began assuming 90% of the business of each of the remaining Bristol West Holdings, Inc. insurance companies: Bristol West Insurance Company (Ohio), Bristol West Casualty Insurance Company (Ohio), Bristol West Preferred Insurance Company (Michigan), and Security National Insurance Company (Florida).

Effective July 1, 2009, a 100% quota share cession agreement was entered into between 21st Century North American Insurance Company (formerly American International Insurance Company), New York, and the Exchange. This quota share agreement was approved by the CDI on June 30, 2009.

Ceded

Affiliated

The Exchange maintained certain fronting 100% quota share agreements (the so-called "RAS" treaties, which are historically long-standing reinsurance agreements with affiliates initiated variously between 1950 and 1995) by which all of the property business it wrote was ceded "prior to the intercompany pooling" to Fire Insurance Exchange. Similarly all of its workers' compensation, medical malpractice, and commercial lines business was ceded to Truck Insurance Exchange via the RAS quota share treaties.

Other affiliated reinsurance cessions that the Exchange engaged in during the examination period included an auto physical damage (APD agreement) 100% quota share agreement, effective January 1, 2006, with two affiliates: Zurich Insurance Company (Zurich) and Farmers Reinsurance Company (Farmers Re). The premium for this APD agreement was $1 billion annually with Zurich assuming an 80% participation and Farmers Re assuming a 20% participation. The CDI approved this agreement on December 28, 2005. This 2006 APD agreement was renewed with the same terms, effective January 1, 2009, for a three-year term. The CDI approved this latest APD agreement on April 27, 2009.

The Exchange is a party to an "all-lines" quota share reinsurance agreement ceding business to Zurich and Farmers Re. The agreement as amended, effective December 31, 2005, ceded a 6% quota share (Zurich 4.8% and Farmers Re 1.2%). The CDI approved this 2005 amendment on December 28, 2005. The agreement was amended, effective December 31, 2007, to decrease the percentage to 5% (Zurich 4% and Farmers Re 1%) and extend the duration to December 31, 2010. The 2007 amendment was approved by the CDI on December 28, 2007. An amendment, effective September 30, 2008 increased the percentage to 25%. This 25% all lines quota share agreement was then terminated, effective June 30, 2009, and replaced with a new 37.5% all lines quota share agreement (Zurich 30% and Farmers Re 7.5%). An amendment, effective December 31, 2009, decreased the percentage ceded to 35%. The CDI approved the December 31, 2009, amendment to this agreement on May 25, 2010.

Effective January 1, 2000, the Exchange entered into a Retrocession Agreement with Foremost I.C. through which the Exchange retroceded to Foremost I.C. 95% of mobile home, manufactured homes and recreational vehicle business concurrently ceded by Foremost I.C. under the reinsurance agreement. The Exchange retained business (assumed from Foremost I.C.) other than insurance on mobile homes, manufactured homes, and recreational vehicles. The CDI approved this agreement on August 10, 2000.

<u>Ceded</u>

<u>Non-affiliated</u>

Treaties ceding risks to non-affiliated reinsurers were written with the Exchange and all of its subsidiaries and affiliates as the cedents. The following is a summary of the principal non-affiliated ceded excess of loss reinsurance treaties inforce as of December 31, 2009:

Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Maximum Limits
Property Catastrophe Excess of Loss – 1st Layer	Lloyds of London (32.175%) Various reinsurers (59.28%)	$250 million per occurrence	91.445% of $200 million excess of $250 million retention per occurrence. Coverage for property located in all territory except Florida.
Property Catastrophe Excess of Loss – 2nd Layer	Various reinsurers (95%)	$450 million per occurrence	95% of $550 million excess of $450 million retention per occurrence.
Regional Property Catastrophe Excess of Loss	Lloyds of London (20.856%) Various reinsurers (74.144%)	$1 billion per occurrence	95% of $500 million excess of $1 billion retention per occurrence. Coverage for property located Texas, Louisiana, Arkansas, Oklahoma, and California.
Property Catastrophe Excess of Loss – 1st Layer Texas Only	Flagstone Reinsurance Limited (12%) Partner Reinsurance Company, Ltd. (11%) Various reinsurers (72%)	$1.5 billion per occurrence	95% of $300 million in excess of $1.5 billion per occurrence. Coverage for property located in Texas only.

Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Maximum Limits
Property Catastrophe Excess of Loss – 2nd Layer Texas Only	Flagstone Reinsurance Limited (12%) Partner Reinsurance Company, Ltd. (11%) Various reinsurers (77%)	$1.8 billion per occurrence	100% of $200 million in excess $1.8 billion retention per occurrence. Coverage for property located in Texas only.
Property Catastrophe Excess of Loss – Southeast region	DaVinci Reinsurance, Ltd. (17%) Renaissance Reinsurance, Ltd (17%) Validus Reinsurance, Ltd. (15%) Lloyd's of London (33.5%) Various reinsurers (17.5%)	$200 million per occurrence.	100% of $200 million in excess of $200 million retention per occurrence. Coverage for losses from Alabama, Florida, Georgia, North Carolina and South Carolina.
Property Catastrophe Excess of Loss	Lloyds of London (33.5%) Various reinsurers (67.5%)	$20 million per occurrence.	100% of $80 million in excess of $20 million in any one occurrence. Coverage for Zurich Small Business Solutions' losses from Florida only.
Property Catastrophe Umbrella Excess of Loss	Lloyds of London (23.33%) Various reinsurers (76.67%)	$1 billion per occurrence.	100% of $300 million in excess of $1 billion per occurrence. Coverage for losses from Alabama, Arkansas, Kentucky, Louisiana, Mississippi, Missouri, Oklahoma, Tennessee, and Texas.
Property Per Risk Excess of Loss – 1st Layer	Lloyds of London (47%) Various reinsurers (53%)	$3 million per risk	100% of $7 million in excess of $3 million per risk and $7 million in aggregate losses.
Property Per Risk Excess of Loss – 2nd Layer	Lloyds of London (50.9%) Various reinsurers (49.1%)	$10 million per risk	100% of $40 million in excess of $10 million per risk.
Property Per Risk Excess of Loss – 3rd Layer	Lloyds of London (58%) Various reinsurers (42%)	$50 million per risk	100% of $25 million in excess of $50 million per risk.

Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Maximum Limits
Casualty / Workers Compensation Catastrophe Excess of Loss – 1st Layer	Lloyds of London (32%) Aspen Insurance UK Limited (20%) Endurance Specialty Ins. Ltd. (25%) Various reinsurers (23%)	$10 million per occurrence	100% of $15 million in excess of $10 million per occurrence.
Casualty / Workers Compensation Catastrophe Excess of Loss – 2nd Layer	Lloyds of London (41%) Endurance Specialty Ins. Ltd. (26%) Various reinsurers (33%)	$25 million per occurrence.	100% of $25 million in excess of $25 million per occurrence.
Casualty / Workers Compensation Catastrophe Excess of Loss – 3rd Layer	Lloyds of London (24.69%) Aspen Insurance UK Limited (18.74%) Endurance Specialty Ins. Ltd. (26.15%) Various reinsurers (30.42%)	$50 million per occurrence.	100% of $50 million in excess of $50 million per occurrence.
Workers Compensation Catastrophe Excess of Loss	Lloyds of London (17%) Montpelier Reinsurance Ltd. (20%) Tokio Millennium Reinsurance Limited (25%) Validus Reinsurance, Ltd. (15%) Various reinsurers (13%)	$50 million per occurrence.	90% of $50 million in excess of $100 million per occurrence.
Marine Yacht Excess of Loss – 1st Layer	Swiss Reinsurance America Corp. (32.5%). Transatlantic Reinsurance Company (15%)	$5 million per occurrence	100% of $5 million in excess of $5 million per occurrence.

Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Maximum Limits
	Various reinsurers (52.5%)		
Marine Yacht Excess of Loss – 2nd Layer	Swiss Reinsurance America Corp. (32.5%). Transatlantic Reinsurance Company (15%) Various reinsurers (52.5%)	$10 million per occurrence.	100% of $10 million in excess of $10 million per occurrence.
Marine Yacht Excess of Loss – 3rd Layer	Swiss Reinsurance America Corp. (32.5%). Transatlantic Reinsurance Company (15%) Various reinsurers (52.5%)	$10 million per occurrence.	100% of $10 million in excess of $20 million per occurrence.

As of December 31, 2009, reinsurance recoverables for all ceded reinsurance totaled $14.9 billion, or 248% of surplus as regards policyholders. Of the reinsurance recoverables 78.3% were from admitted affiliates, primarily resulting from the pooling arrangement of which the Exchange was the lead company, and 21.2% were from Zurich Insurance Company, a non-admitted affiliate.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2009

Underwriting and Investment Exhibit for the Year Ended December 31, 2009

Reconciliation of Surplus as Regards Policyholders
from December 31, 2006 through December 31, 2009

Statement of Financial Condition
as of December 31, 2009

Assets	Ledger and Nonledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$ 6,708,424,602	$	$ 6,708,424,602	
Stocks:				
Preferred stocks	5,727,479		5,727,479	
Common stocks	3,559,042,717		3,559,042,717	
Real Estate				
Properties occupied by the company	42,794,501		42,794,501	
Properties held for the production of income	735,195		735,195	
Properties held for sale	1,826,389		1,826,389	
Cash, cash equivalents and short-term investments	936,160,786		936,160,786	
Other invested assets	9,222,536		9,222,536	
Receivable for securities	41,093		41,093	
Aggregate write-ins for invested assets	5,354,743		5,354,743	
Investment income due and accrued	62,958,731	87,443	62,871,288	
Premiums and consideration:				
Uncollected premiums and agents balances in the course of collection	389,257,725	51,977,590	337,280,135	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	1,624,136,389		1,624,136,389	
Accrued retrospective premiums	1,967,276		1,967,276	
Reinsurance:				
Amounts recoverable from reinsurers	657,776,721		657,776,721	
Net deferred tax asset	346,679,434	70,607,827	276,071,607	
Guaranty funds receivable or on deposit	2,173,207		2,173,207	
Electronic data processing equipment and software	7,222		7,222	
Furniture and equipment, including health care delivery assets	3,259,095	3,259,095		
Receivables from parent, subsidiaries and affiliates	775,337,452		775,337,452	
Aggregate write-ins for other than invested assets	14,625,467	4,979,959	9,645,508	
Total assets	$15,147,508,760	$130,911,914	$15,016,596,846	

Statement of Financial Condition
as of December 31, 2009

(Continued)

Liabilities, Surplus and Other Funds

Losses		$ 3,010,354,284	(1)
Reinsurance payable on paid losses and loss adjustment expenses		1,218,410,077	
Loss adjustment expenses		954,116,084	(1)
Commissions payable, contingent commissions and other similar charges		6,862,825	
Other expenses		288,332	
Taxes, licenses and fees		7,495,947	
Current federal and foreign income taxes		26,844,050	
Unearned premiums		2,176,034,986	
Advance premium		50,790,222	
Dividends declared and unpaid: Policyholders		1,592,124	
Ceded reinsurance premiums payable		432,101,010	
Funds held by company under reinsurance treaties		3,182,269,575	
Amounts withheld or retained by company for account of others		10,392,819	
Remittances and items not allocated		84,756,161	
Provision for reinsurance		967,149	
Aggregate write-ins for liabilities		154,081,021	
Total liabilities		11,317,356,666	
Surplus notes	$1,760,675,000		
Unassigned funds (surplus)	1,938,565,180		
Surplus as regards policyholders		3,699,240,180	
Total liabilities, surplus and other funds		$15,016,596,846	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2009

Statement of Income

Underwriting Income		
Premiums earned		$5,261,376,079
Deductions:		
Losses incurred	$2,904,936,110	
Loss adjustment expenses incurred	648,029,574	
Other underwriting expenses incurred	1,638,002,195	
Total underwriting deductions		5,190,967,879
Net underwriting gain		70,408,200
Investment Income		
Net investment income earned	$ 151,275,011	
Net realized capital gains	1,500,430	
Net investment gain		152,775,441
Other Income		
Net loss from agents' or premium balances charged off	$ (53,557,975)	
Finance and service charges not included in premiums	43,969,761	
Aggregate write-ins for miscellaneous loss	(132,013,998)	
Total other income		(141,602,212)
Net income before dividends to policyholders, before all other federal and foreign income taxes		81,581,429
Dividends to policyholders		901,405
Federal and foreign income taxes incurred		22,861,437
Net income		$ 57,818,587

Underwriting and Investment Exhibit
for the Year Ended December 31, 2009

(Continued)

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2008		$3,253,883,058
Net income	$ 57,818,587	
Change in net unrealized capital gains less capital gains tax	361,238,345	
Change in net deferred income tax	3,486,327	
Change in nonadmitted assets	1,708,740	
Change in provision for reinsurance	2,184,434	
Change in surplus notes	65,000	
Cumulative effect of changes in accounting principles	4,793,899	
Aggregate write-ins for gains in surplus	14,061,790	
Change in surplus as regards policyholders		445,357,122
Surplus as regards policyholders, December 31, 2009		$3,699,240,180

Reconciliation of Surplus as Regards Policyholders
from December 31, 2006 through December 31, 2009

	Gain in Surplus	Loss in Surplus	
Surplus as regards policyholders, December 31, 2006, per Examination			$3,148,567,064
Net income	$180,240,439	$	
Change in net unrealized capital gain	142,385,429		
Change in net deferred income tax		17,879,711	
Change in nonadmitted assets		74,753,324	
Change in provision for reinsurance		14,828	
Change in surplus notes	300,195,000		
Cumulative effect of change in accounting principles	4,793,899		
Aggregate write-ins for gain in surplus	15,706,212		
Totals	$643,320,979	$92,647,863	
Net increase in surplus as regards policyholders for the examination			550,673,116
Surplus as regards policyholders, December 31, 2009, per Examination			$3,699,240,180

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

The Exchange was directed by the California Department of Insurance (CDI), under California Insurance Code (CIC) Section 733(g), to retain the American Actuarial Consulting Group, LLC, (AACG) for the purpose of assisting this examination in determining the reasonableness of the Exchange's loss and loss adjustment expense reserves. Because the business of the Farmers property and casualty companies was pooled, it was necessary to review the losses on a group-wide basis. Based on the analysis by AACG and the review of their work by a Casualty Actuary from the CDI, the Exchange's December 31, 2009 reserves for losses and loss adjustment expenses were determined to be reasonably stated and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None

Previous Report of Examination

Management and Control - Claims Adjustment Services Arrangement (Page 13): The claims adjustment services arrangement between the Exchange and certain of its affiliates (the pooled companies), with the Exchange providing all of their claims adjustment services was not written. It was recommended that the Exchange, and all of its California-domiciled affiliates that the Exchange is providing claims adjustment services to, enter into a written claims adjustment services agreement and submit it to the California Department of Insurance (CDI) for approval pursuant to California Insurance Code (CIC) Section 1215.5. The Exchange, and certain California-domiciled affiliates that the Exchange had provided claims adjustment services to, have subsequently entered into CDI approved management services agreements that include claims adjustment services.

Management and Control - Managed Care Services Agreement (Page 13): Zurich Services Corporation (ZSC), an affiliate, provided certain bill review and medical management services for the Exchange's workers' compensation claims. It was recommended that the Exchange submit the managed care services agreement to CDI for approval pursuant to CIC Section 1215.5. The submission of the ZSC managed care services agreement was still pending as of this examination date, December 31, 2009. The Exchange and ZSC have, via amendment, terminated this agreement (except for case management services) effective July 15, 2010. A replacement managed care services agreement with Corvel Healthcare Corporation (non-affiliated) is currently near completion.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Exchange's officers and employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

______/S/________________

Gary W. McMurray, CFE
Examiner-In-Charge
Contract Insurance Examiner
Department of Insurance
State of California